

THE BENEFITS OF LIFE INSURANCE TRUSTS

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At an individual's death it is possible that his or her estate could be subject to taxes in excess of fifty percent. Consequently, more than fifty cents of every dollar accumulated during an individual's lifetime can go to Uncle Sam and the State of New Jersey upon death. Unfortunately, the bad news does not end there. The IRS demands, in most cases, that the estate tax be paid within nine months of a person's date of death. Frequently, an estate does not have cash or other liquid assets readily available for payment of the Federal or State Estate Tax. Taxing authorities do not want to receive a partial interest in real estate or a family business. If payments cannot be made on a timely basis then late filing penalties and interest charges may occur. If your family would be faced with this dilemma then you should consider purchasing life insurance.

Most people consider life insurance to be a necessity when their children are young. Once children move out of a home parents often reduce their life insurance coverage. Individuals with estates in excess of \$675,000 fail to realize that life insurance can be a great vehicle for providing ready cash necessary to pay Federal and State Estate Taxes. Furthermore, life insurance gets favorable treatment under the Internal Revenue Code. If an individual does not own or control a policy on his or her life, and the proceeds are not payable to the individual's estate, the insurance proceeds will not be included in the estate. Therefore, the beneficiaries of the policy can receive the insurance proceeds tax-free.

Most married individuals have life insurance policies with the insured designated as owner and the surviving spouse listed as beneficiary. The proceeds from the policy will be included in either the decedent's estate, when he dies, or the spouse's estate. Some clients try to get around this problem by naming their children as owners and beneficiaries of their insurance policies. However, problems could arise if a child gets into financial trouble or predeceases the insured. Furthermore, the surviving spouse will not have access to any of the life insurance proceeds. Generally, this is not consistent with the estate plans of most married clients.

A great way to get around these problems, yet still shield the life insurance proceeds from estate tax, is to place the policy in a trust. The trust becomes both the owner and the beneficiary of the policy. When the insured dies, the Trustee collects the insurance proceeds on behalf of the trust, and reinvests or distributes the monies in accordance with the terms of the trust. The trust can remain in effect after an individual's death. Often married couples provide for the surviving spouse to have access to income and principal during

their lifetime, with principal distributed to the children upon the surviving spouse's death. If a trust is set up properly then assets inside the trust will be excluded from the surviving spouse's estate. Potentially this can avoid Federal and State Estate Tax from being due.

Although a life insurance trust presents a great way to save estate taxes, it does have drawbacks. One major disadvantage is that the trust is irrevocable. The terms of the trust cannot be altered or amended once executed. Second, the previous owner of the policy must relinquish control over the insurance. That means that the insured cannot be the trustee. It is typically recommended that a family member, bank or trust company be named trustee.

In conclusion, life insurance trusts can save Federal and State Estate Taxes, provide protection from creditors, and still give a surviving spouse access to insurance proceeds. If you have existing life insurance and your estate exceeds \$675,000 then you should contact an estate planning attorney to discuss the benefits of an irrevocable life insurance trust.